



**PUBLIC COMMENTS OF THE ELECTRONIC FRONTIER FOUNDATION
REGARDING INVESTIGATION OF PATENT ASSERTION ENTITIES**

PAE Reports: Paperwork Comment; Project No. P131203

**Submitted on June 18, 2014 to the Federal Trade Commission and the
Office of Information and Regulatory Affairs, Office of Management and Budget**

The Electronic Frontier Foundation (“EFF”) welcomes the FTC’s interest in patent assertion entities (PAEs) and is grateful for this opportunity to comment. The Electronic Frontier Foundation is a non-profit civil liberties organization that has worked for more than 20 years to protect consumer interests, innovation, and free expression in the digital world. Founded in 1990, EFF represents more than 27,000 contributing members. EFF and its members have a strong interest in promoting balanced intellectual property policy that serves both public and private interests. Through litigation, the legislative process, and administrative advocacy, EFF seeks to promote a patent system that facilitates, and does not impede, “the Progress of Science and useful Arts.”

I. Summary

EFF welcomes the FTC’s decision to go forward with a Section 6(b) study. EFF strongly supports the FTC’s efforts to investigate the behavior and economic impact of PAEs. The FTC is well-placed to investigate in the public interest with respect to patents. In addition to helping the FTC itself, empirical data will assist the courts, Congress, and the USPTO to craft the most appropriate response to the rapid growth of PAE litigation. EFF believes the proposed information requests are consistent with the Paperwork Reduction Act, 44 U.S.C. §§ 3501 et seq. and should proceed.

II. There is a pressing need for empirical data about the activities of PAEs.

An FTC study is particularly important because it will collect information not usually available to the public. While some litigation data is available, much patent assertion activity

takes place in the shadows. Demand letters—which vastly outnumber lawsuits¹—are rarely made public. And settlements generally include non-disclosure agreements. EFF has worked to create more transparency regarding patent demand letters. In July 2013, we launched a public database of letters and invited companies to submit PAE demands.² But only a tiny percentage of demand letters are available.

Further, a great deal of PAE activity is “hidden beneath a labyrinth of shell companies.”³ This creates a number of problems. First, “potential targets find it difficult to engage in licensing negotiations with entities that have no ‘website, employees, or offices.’”⁴ This means “it is ‘difficult or impossible to call someone’ and ‘have a conversation about licensing fees.’”⁵ Moreover, the portfolio seeking to be licensed “could consist of ‘weak, overbroad patents’” but due to the lack of information makes it “nearly impossible to know what the licensee is getting for its money.”⁶ The justifications PAEs put forth for obscuring their information have “little direct connection to promoting innovation and much effect in shrouding crucial relationships in secrecy.”⁷

¹ Just two PAEs have combined to send approximately 30,000 demand letters to small businesses around the country. See Mark Chandler, *Innovatio Case: Victory for Cisco Customers Makes the Case for Patent Reform*, Cisco Blogs (Feb. 6, 2014 9:48 AM), at <http://blogs.cisco.com/news/innovatio-case-victory-for-cisco-customers-makes-the-case-for-patent-reform/> (PAE called Innovatio IP Ventures sent 14,000 demand letters); Julie Samuels, *MPHJ Exposed: The Real Dirt on the Notorious Scanner Troll* (Jan. 14, 2014), at <https://www.eff.org/deeplinks/2014/01/mphj-exposed-the-real-dirt-notorious-scanner-troll> (PAE called MPHJ sent over 16,000 demand letters).

² *Trolling Effects*, www.trollingeffects.org

³ Michael A. Carrier, *Patent Assertion Entities: Six Actions the Antitrust Agencies Can Take* at 3 (Jan. 30, 2013), CPI Antitrust Chronicle, Winter 2013, Vol. 1 No. 2, at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2209521; see also Tom Ewing & Robin Feldman, *The Giants Among Us*, 2012 Stan. Tech L. Rev 1, 26 (2012), at <http://stlr.stanford.edu/pdf/feldman-giants-among-us.pdf>

⁴ Carrier, *Patent Assertion Entities* at 3 (citing Matthew Rappaport & Lily Li, *How Hidden IP Assets Hurt the Entire Patent Community*, LAW360, at 2 (Nov. 28, 2012)).

⁵ *Id.*

⁶ *Id.* at 4.

⁷ *Id.*

Since the FTC first proposed doing a study on PAEs, interest in patent reform has built. The Innovation Act passed the House on December 5, 2013 with a vote of 325-91. While reform has currently stalled in the Senate, legislation is still possible. Considering that many opponents of patent reform have argued that the negative impact of PAEs has been overstated,⁸ a better understanding of PAE activities will help policymakers craft an appropriate response.

III. The FTC is uniquely placed to investigate PAE activity.

The FTC is well-placed to investigate in the public interest with respect to patents and PAE activities. The FTC has already released two successful reports on the patent system: *To Promote Innovation: The Proper Balance of Competition*⁹ and *Patent Law and Policy and The Evolving IP Marketplace: Aligning Patent Notice and Remedies with Competition*,¹⁰ respectfully. Those reports have been widely cited and indeed influential both in the courts and among policy makers. For instance, our research shows that more than 500 secondary sources, such as law review articles and legal treatises, and many courts—including the Supreme Court¹¹—have cited the 2003 report. Likewise, more than 40 secondary sources and at least one federal court¹² have thus far cited the 2011 report.

⁸ See, e.g., Eric Cohen, *What Is Really Needed In Patent Reform*, Law360 (April 07, 2014), at <http://www.law360.com/articles/525750/what-is-really-needed-in-patent-reform>; Peter J. Toren, *Who You Calling a 'Patent Troll'? Term is Overused, Harm Overblown*, National Law Journal (March 18, 2014).

⁹ Available at: <http://www.ftc.gov/os/2003/10/innovationrpt.pdf>

¹⁰ Available at: <http://www.ftc.gov/os/2011/03/110307patentreport.pdf>

¹¹ See, e.g., *eBay v. MercExchange, LLC*, 547 U.S. 388, 396 (2006); *Laboratory Corp. of America Holdings v. Metabolite Labs., Inc.*, 548 U.S. 124, 134 (2006); *Microsoft Corp. v. i4i Ltd. P'ship*, 131 S. Ct. 2238, 2252 n.11 (2011).

¹² *Cascades Computer Innovation LLC v. RPX Corp.*, 2013 WL 316023 at *1 n.3 (N.D. Cal. Jan. 24, 2013).

IV. The modest costs associated with the FTC study are justified in light of the huge economic impact of PAE activity.

The FTC estimates between 425 and 845 hours for each patent assertion entity to prepare a response. This is comparable to other Section 6(b) studies.¹³ While the study will impose a modest burden on some PAEs, this is dwarfed by the impact PAEs have on the economy. In 2011, PAE litigation imposed approximately \$29 billion in direct costs (such as settlements and legal fees) on operating companies.¹⁴ Researches have estimated that PAE “lawsuits are associated with half a trillion dollars of lost wealth to defendants from 1990 through 2010” and that this “lost wealth has averaged over \$80 billion per year.”¹⁵ Evidence also suggests that PAEs mostly target operating companies that have independently developed the technology at issue.¹⁶ Also, PAE-based litigation has inhibited venture capital investment in startups, costing between hundreds of millions to billions of dollars over the last five years.¹⁷ It appears that the huge costs imposed by PAEs are deadweight losses for the economy and deliver very few benefits to inventors.¹⁸

Most economic research regarding PAEs has focused on litigation activity since that data is public. To the extent this research ignores demand letters and pre-suit settlements, these

¹³ See, e.g., 76 Fed. Reg. 73,640, 73,643 (Nov. 29, 2011) (estimating respondents would spend approximately 300 and 620 hours and \$186,000 per company responding to a Section 6(b) request concerning alcohol advertising).

¹⁴ Brian T. Yeh, Cong. Research Serv., R42668, *An Overview of the “Patent Trolls” Debate*, at Summary and 2 (2012).

¹⁵ James Bessen et al., *The Private and Social Costs of Patent Trolls*, Regulation, Winter 2011–2012, at 26.

¹⁶ Christopher A. Cotropia & Mark A. Lemley, *Copying in Patent Law*, 87 N.C. L. Rev. 1421, 1459 (2009) (“Virtually every case filed—and even the overwhelming majority of those in which the plaintiffs win and claim that the defendant was a willful infringer—involve not theft or even copying with a legitimate effort to design around but independent development by the defendant.”)

¹⁷ Catherine E. Tucker, *The Effect of Patent Litigation and Patent Assertion Entities on Entrepreneurial Activity* (May 15, 2014), at: <http://cdn.arstechnica.net/wp-content/uploads/2014/06/Tucker-Report-5.16.14.pdf>

¹⁸ Cotropia & Lemley at 28 (noting that “very little of this loss of wealth represents a transfer to inventors”).

estimates may understate the impact of PAEs. The FTC's proposed study should help complete the picture.

It should also be noted that the PAE business model – acquiring and asserting patents – relies entirely on the exploitation of government-granted rights. In essence, PAE's are “opportunistic litigation mills” that “cloak themselves in the legitimacy of patents.”¹⁹ To the extent PAE activity is wasteful or abusive, it will require a government response (either by the USPTO, Congress, the courts, or the FTC). This makes it a particularly appropriate topic for a government study.²⁰

V. Conclusion

EFF again thanks the FTC and the OMB for the opportunity to comment on the proposed Section 6(b) study. EFF strongly supports the FTC's efforts to research and better understand PAE behavior. The proposed investigation should proceed.

Respectfully submitted,

/s/

Electronic Frontier Foundation

Daniel Nazer

Staff Attorney and The Mark Cuban Chair to Eliminate Stupid Patents

Vera Ranieri

Staff Attorney

Michael Barclay

Special Counsel

June 18, 2014

¹⁹ Robert P. Merges, *The Trouble with Trolls: Innovation, Rent-Seeking, and Patent Law Reform*, 24 Berkeley Tech. L.J. 1583, 1599 (2009).

²⁰ It is notable that organizations in favor of limited government, such as the Washington Legal Foundation, support the FTC's actions here. *See* http://www.ftc.gov/sites/default/files/documents/public_comments/2013/12/00074-87884.pdf